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Financial Literacy; What do College Age Students Know About Personal Finance

Financial literacy is something that many people debate in todays day and age. This word *financial literacy* gauges the knowledge of people in terms of personal finance so things like credit cards, loans, how macro and micro economics events effect them and savings. While these are not the only things in the realm of personal finance these are they key points I want to hone in on on. I conducted a survey of over fifty college students ages 18-22 that had questions to gauge financial literacy. Upon getting the results I analyzed them by response to create data to present. (Ask what to add in this paragraph)

Financial literacy is one of the most crucial educational pieces for life in the real world and for 18-22 years olds in this generation it is not taught in high school or college. Most learn financial literacy through parents or trial and error. This is scary thought, because these decisions you make at 18-22 could potentially haunt you the rest of your life. Many students lack the basic knowledge of budgeting, how debt works and what an emergency fund is. Knowing these few things can help you make educated decisions in college that are fiscally responsible.

The importance of financial literacy lies in the idea that your uneducated decisions you make now can effect your educated decisions later in life. What this means is as you grow older you may learn by trial and error which a lot of people do. So mistakes are made in college and they learn from mistakes and deal with the negative consequences of the mistakes and make sure not to repeat them. Some though make these mistakes and never recover because they don’t realize they are making a mistake and by the time they do it is too late. Another scenario is not capitalizing on opportunity. This is not something that will effect your life in a negative way, it may be a regret later in life, but that is apart of the learning process I was talking about previously. An example of this is investing at a young age. Time is the biggest asset college kids have in terms of personal finance. What I mean by this is say you invest in a Roth IRA which is an individual retirement account your potential return by the time you are in your sixties could be millions. Here is an example of this theory. At age 18 someone invest 5,000 dollars and every year after that until they hit 65 they continue this 5000-dollar yearly contribution at a 7 percent return rate this said person will have roughly 1.7 million dollars in this account. As a financial advisor last summer I learned that this account is after tax money so when you draw on it it is completely tax free. If you have never heard of this and it peaks your interest as something you should do or if you feel like you have missed the opportunity you now understand why financial literacy is so important.

Secondary Research

Financial literacy is a growing problem in the United States. This is a very broad statement because financial literacy can mean a number of things. An area that is effecting people from 18-22 more than ever is student loans. This is the age when you are either going to college or finishing up which may mean student loans. In the United states there is currently 1.1 trillion dollars’ worth of student loans outstanding and the average student accruing more than 26,000 in debt upon graduation. (Bidwell, 2013) While this number is large the more alarming statistic is that more than half of this is not paid back because students are struggling financially. Where financial literacy falls is the students that are getting these loans not knowing what they are getting themselves into. They do not read the fine print or just flat out don’t know they just sign where they are told and decide they will worry about it when the time comes. There are many programs out there for student loans that are underutilized and the cause for this is financial illiteracy.

Another issue with student loans is the repercussions of defaulting on your loans. In Allie Bidwell’s article Student Loan Default Rates Rise for Sixth Year she states that The national two-year cohort default rate rose from 9.1 percent in fiscal year 2010 to 10 percent in the fiscal year 2011. Similarly, the three-year cohort default rate rose from 13.4 percent in 2009 to 14.7 percent in 2010. (Bidwell, 2013) The people defaulting on these loans are negatively effecting their future. They are effecting their credit scores which in turn make it hard to get loans or a mortgage for your house. In a way these people are not only effecting themselves on a microeconomic level, but they are effecting America on a macroeconomic level. The reasoning behind this is they are unable to get loans or buy a house which stimulates the economy because they are spending money which means someone else is making money and spending money. This cycle is what keeps America going and if people are unable to get loans or mortgages how are they spending money.

Being finically literate can really help negate the negative effects of student loans. A few statistics on how being financially illiterate can effect you in the long run aside from paying them off for years is putting things off. A recent survey from a non profit called American student assistance found nearly three-quarters of students said they've put off saving for retirement because of student debt. Another 43 percent said they've delayed starting a family and 27 percent said they found it difficult to buy daily necessities because of loan payments. (Bidwell, 2013) This is alarming, if you put off retirement because of loans you wont start until late and that can cause you to have to work longer. On a macroeconomic level this effects everyone because the work force will be working until they are older do to lack of retirement funds which means younger people who are fresh out of college will not have as many job opportunities which will cause the vicious cycle to restart.

Financial literacy in college freshmen is alarming, the majority of high schools do not require a finance course in high school. Because of this students are unable to answer simple questions like the ones that follow:

According to College freshmen flunk financial literacy 101 an article by Jillian Berman

“on average, freshmen at four-year colleges could only answer about two out of six questions correctly about topics like the right amount of money to set aside in case of a financial emergency, the conditions placed on student loan borrowers and how long a late payment remains on your credit history” (Berman, 2015)

More often than not these students are living on their own for the first time and they have no clue about these basic financial ideas. This is the future of America, in a time where we are plagued by debt in the forms of loans and credit cards it would make sense to mandate some sort of financial literacy course to try and combat this ongoing issue. While often times these kids are learning by experience, it would be less costly to the individual if people were learning in a proactive manner as opposed to reactive manner.

According to a survey conducted by Everfi called Money Matters on Campus, of the 42,000 surveyed only 39% of students enrolled in a 4-year college use a budget. (Sherman, 2015) A budget is one of the first things that comes to peoples mind when they think of personal finance and hardly any of these college students are using them. Creating and following a budget not only helps you save money, but it creates good spending habits for the future. Many people do not use a budget either because they don’t know ho or they are too lazy. Financial literacy and understanding the importance of using a budget properly can help create drive and commitment to doing a budget. I challenge you to track your spending every expense and revenue for one month and see if that makes you want to become a more frugal person. If not, then continue using a budget anyway it could help in the long run.

Before I move into the research I conducted I am going to give the professional answers to a few of the questions that I asked. First, does carrying a balance on your credit card help your credit. The advice given by Erik Carter is paying them off in full is the best way to build a positive credit score. While paying them off in whole may not be feasible as long as you pay the minimum balance on time your score wont be hurt. The problem with this is the interest payments you incur. Next, I asked if you should pay down your largest debts first. This is smart because you may be charged a lower interest but since the loan for example mortgage are so large the small percent is still a big number. These are the answers to only a few of the questions I asked. The rest were questions that gauged financial literacy based of of these questions.

Primary Research

The research I conducted was through a survey. I asked for age, field of study, gender and if they are a first generation college student. These questions were used as a factor of comparison for my research. What this means is I broke the data up into each of the categories and compared results to come up with demographical data. I compared the data as a whole then broke it down to further understand the financial literacy rate of the above factors. I created the rest of the questions based of knowledge I obtained last summer as a financial advisor and online sources. I personally crafted each question to pertain to the demographic I was gathering data on. After I created the survey I sent this survey to my fraternity, class and other friends that I have that fit the age range of 18-23. My other friends ranged from students in Greek life and students that just go to school. I wanted to make sure I covered all types of people that way the data was not skewed.

The reason I wanted to obtain this data is to find how financially literate people were in the age range of 18-23, stemming from this I wanted to find out the financial literacy of Central Michigan students that fit the age demographic. As I have previously stated to find this out I created a survey that was carefully crafted to bring in meaningful data pertaining to the literacy level, financially, in college age students. I found out that Central Michigan students are financially literate in terms of personal finance. There was a lot of indicators that students new what they were talking about. I put in a couple open ended questions to ensure participants were not just getting lucky and guessing the correct answer or backing into an answer.

DISCUSION OF FINDINGS

Financial literacy is the single most important thing that students can learn in life. You may ask the reasoning behind this, well its simple money is what makes the world go around and if you are not literate when it comes to using money or things that pertain to money you are hurting yourself and possibly everyone else. An example of this is the great recession that was caused because many big banks failed do to the amount of defaults on housing loans. The reason for these defaults was partially financial illiteracy and partially lack of regulators doing their job. The kicker is if people were financially literate there would have been less of a need for regulators and the people buying homes they could not afford. Inflating rates on their loans kicked in after 2 to 3 years of paying on the loan and they could no longer afford the rates of their house or houses. The default on loans crippled big banks and sent America into a downward spiral known as the great recession. The reason I bring this up is student loans. The excessive amount of strident loans outstanding leaves some financial experts weary of a “student loan crisis” that has similar effects of the housing market crash. In John Marino’s article some on Wall Street say $1.2 trillion in student debt could trigger the next market crash famous hedge fund manager Bill Ackman says “There is a crisis in the student loan business and this crisis could tank the economy.” (Marino, 2015) This is because many are already overwhelmed with debt in the form of loans that they got. If they knew what they were getting themselves into, being financially literate, they may have went about things differently. According to my research

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